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THE GOVERNMENT OF LESOTHO GETS US$61.4 MILLION FROM THE INTERNATIONAL MONETARY FUND (IMF) UNDER THE EXTENDED CREDIT FACILITY

As most countries around the globe recover from the scars of the global financial crisis and the subsequent systemic economic contractions and while they are faced with various challenges, the IMF extends its role of helping them deal with their various macroeconomic problems………

Background

Over several decades, the IMF has developed various loan instruments or "facilities" that were and are tailored to address specific economic conditions of its diverse members. The programs are designed to help poor, /low-income countries to tackle their macroeconomic problems, particularly, balance of payments (BOP) problems. Until 1999, the IMF was running a facility known as Enhanced Structural Adjustment Facility (ESAF). The ESAF was replaced by the Poverty Reduction and Growth Facility (PRGF), the aim of which was to enhance poverty reduction and to promote sustainable economic growth in low-income members of the IMF. This was meant to be a lynchpin for a renewed growth-oriented strategy and poverty-reduction. More explicitly, the PRFG was aimed at supporting economic programs in low-income countries in order to strengthen their BOP positions while concurrently fostering sustainable growth, leading to poverty reduction and better standards of living.

INSIDE

Over the years, economic landscape improved and macroeconomic stability strengthened in most of these low-income countries. As a result, the IMF had to upgrade its support facilities in order to align itself with the new macroeconomic developments. However, the countries still experienced low per capita income (a standard measure of poverty). In addition, the global financial crisis that swept from the developed countries across the emerging and developing economies made the IMF lending more critical to low-income countries.

Against this background, new flexible and accommodative facilities were established to address problems facing the low-income countries. The IMF then set up the new Poverty Reduction and Growth Trust with three windows, namely, Extended Credit Facility, Standby Credit Facility and Rapid Credit Facility and they became operational from January 2010.

However, this article focuses exclusively on ECF. It states the rationale for this facility and highlights how it is expected to operate in line with the three-year economic program of the Government of Lesotho.

Does Lesotho need to use the IMF's ECF?

As the storm of financial crisis pillaged across the globe, emanating from the U.S subprime mortgage meltdown, several economies found themselves stacked against the odds. In many countries, including the US and South Africa, employment and other macroeconomic variables veered from positive to negative territories and others deteriorated, leaving trails of poverty and other social ills worse than before the crisis.

Lesotho could not be immune to the effects of the financial crisis and the subsequent economic meltdown, despite several years of economic stability. Economic growth in Lesotho contracted to 1.9 per cent in 2009 from 4.4 per cent realised in 2008. This mainly reflected a marked decline in the textile industry activity. Textile exports declined as a result of repressed demand from the U.S economy. The U.S labour market also deteriorated significantly in 2009 with unemployment rates escalating beyond the single digit in some months. This also affected demand for textile exports negatively. The economy also took hit from the low demand for diamonds exports from Euro area, Lesotho's largest diamond export destination.

In addition, lower household income and a decline in consumption contributed to the economic deterioration in Lesotho. The slump in household income was due to a decline in workers' remittances from South Africa, as Basotho migrant mine workers were being retrenched. The economy also faces a challenge as government revenue declines, largely due to a steep fall in SACU revenue which accounts for a bulk of our revenue.

It is against this backdrop that the Government of Lesotho has deemed it necessary to request a three-year arrangement with the International Monetary Fund under the ECF in a total amount of Special Drawing Rights (SDRs) 41.88 million, with the first disbursement of SDR 7.78 million following the approval of the program. The arrangement is expected to support the Government of Lesotho's medium- term economic objectives and policies

The Extended Credit Facility and the GoL's Medium-Term Economic Program

The ECF arrangement in Lesotho is meant to restore fiscal and external stability, achieve broad-based growth for poverty reduction and to strengthen the financial sector while enhancing access to financial services.

Commencing with the 2010/11 budget, the government has begun to contain recurrent expenditures, the aim of which is to reduce non-productive spending, over the medium-term, to a level consistent with sustainable levels of revenue. The intent is to reduce total expenditure from around 68.0 per cent of GDP in the current fiscal year to around 45.0 per cent in 2015/16. Nonetheless, the government will not compromise spending on critical social programs. To achieve the desired objectives under fiscal consolidation, the specific tools that will be used include: containing the wage bill by restricting new recruitments to high-priority areas; freezing the number of existing positions and reducing the size of the public service and eliminating posts that have been vacant for more than 12 months; reducing spending on goods and services by rationalising diplomatic missions, reducing international travel and cutting expenditure on furniture and equipment.

On the external balance, the government intends to narrow down the current account deficit to about 6.5 per cent of GDP by 2014 as net SACU revenues recover and the fiscal adjustment measures are implemented from a projected deficit of 20.0 per cent of GDP in 2010, owing to steep declines and lower SACU revenues.

The economic program also focuses on broad-based shared-growth and poverty reduction by implementing several structural measures in order to attain the desired objectives. These measures are intended to improve productivity and the investment climate in the country. The improved investment climate will boost competitiveness and productivity by lowering unit labour costs, hence enable the country to attain the growth objectives it is pursuing while concurrently reducing poverty. To this end, the government of the Kingdom of Lesotho, with the assistance of development partners such as Millennium Challenge Corporation (MCC), is pursuing several reforms in these areas. The reforms include: modernization of the civil legal procedures to expedite commercial disputes resolution; reform of land tenure system to facilitate use of land as an economic asset; introduction of the national identity cards; and establishment of the credit Bureau.

In addition, in order to attract increased private sector investment which is conducive for strong and broad-based growth, the government is committed to enhancing investment climate. The effective implementation of private sector competitiveness and diversification program of the World Bank should also help reduce the cost of doing business in Lesotho and boost the country's regional and global competitiveness. To achieve this objective, the government is intending to submit, to parliament, the Companies and Industrial Licensing Bills by the end of September 2010.

The program focuses further on strengthening the financial sector. To this end, the government is intending to deepen the money and capital markets. In particular, the domestic bond market development will assist in extending the yield curve, deepen the securities markets and provide the government with alternative source of finance. The first issue of bonds is intended to be in December, 2010. The Financial Institutions Act (FIA) is being reviewed and amended. It incorporates legal frameworks that underpin the role of the Central Bank of Lesotho's supervision of non-Bank financial institutions, prohibition of unlawful businesses and ponzi schemes. The CBL expects to submit this to parliament by the end of September, 2010. The Financial Intelligence Unit (FIU) is currently being set up in consultation with the development partners and with technical assistance from the US.

Conclusion

There are conflicting views on the economic impact of IMF programs. On the one hand, some argue that higher IMF loan participation rate reduces economic growth and investment. On the other hand, there is evidence that IMF programs can improve BOP and current account balances, lower inflation and increase growth in the long run, as long as the country in question plays its part well in terms of pursuing sound macroeconomic policies aimed at the achievement of the set targets.

In the case of Lesotho, prudent fiscal policy will play a crucial role in determining successful achievement of the program objectives of restoring fiscal and external sustainability which is necessary for high and sustainable economic growth and poverty reduction. Government should continue to pursue containment of fiscal expenditure and maintain international reserves at levels that are conducive for maintenance of the fixed exchange rate regime.

2. NATIONAL FORUM ON AGRICULTURE AND FOOD SECURITY FOR IMPROVING RURAL LIVELIHOODS AND REDUCING POVERTY: "WHAT WORKS AND WHAT DOES NOT AND HOW TO MOVE FORWARD FROM HERE?"

Background

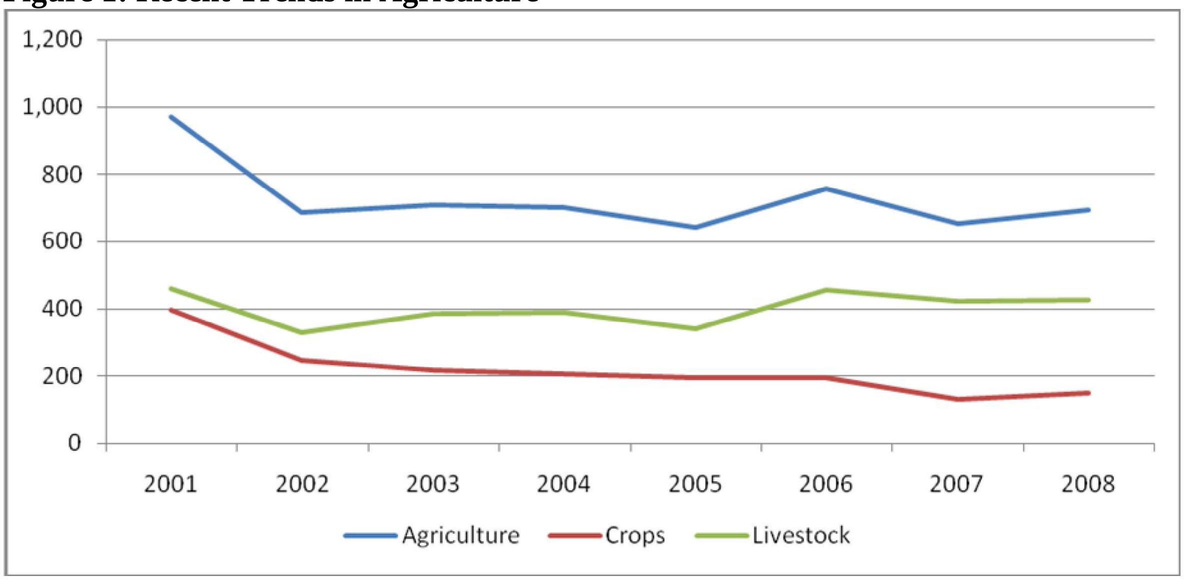
Agricultural production and productivity have declined considerably and, as a result, food insecurity has increased, leading to higher levels of poverty. These declines continued despite several interventions aimed at reviving the agricultural sector. In response to the growing concerns over dwindling agricultural productivity, the Ministry of Agriculture and Food Security (MAFS) called for a National Agricultural Forum to take stock of various challenges facing the sector and to make recommendations and develop a framework through which strategies for reviving the agriculture sector in Lesotho can be implemented. Key stakeholders including relevant government ministries, development partners, farmers, business community took part in this forum.

Overview and Review of Agriculture Subsector

The agriculture subsector is made up of three activities which are crops, livestock and agricultural services. Crops mainly comprise of cereals (Maize, Wheat and Sorghum), beans, peas and other vegetables. Livestock, on the other hand, is mainly constituted by cattle, sheep, goats, piggery and poultry. Finally, services constitute policy development, extension and technical services. Agriculture in Lesotho is mainly characterised by subsistence farming with commercial farming forming only a negligible proportion. Lesotho is a persistent net food importer. Although its main natural resource is water, drought chronically affects the country, forcing the country to appeal for assistance from donors. This illustrates the vulnerability of the sector.

Agriculture used to be the largest subsector in the economy of Lesotho in the early 1980s, but it is now the sixth in terms of contribution to GDP. According to the latest national accounts data set, the share of agriculture to GDP was 7.1 percent in 2008 whereas it was hovering around 21 percent from 1982 to 1987. Since then, the subsector has consistently lost its share due to declining agricultural production coupled with increases in other sectors of the economy. Figure 1 below depicts recent trends in agriculture since 2001. The overall picture portrayed in figure 1 below is a general decline in agriculture as a whole. This decline is more discernible on crops production whereas livestock is fairly constant over the period. The year 2007 was a recent drought year which saw crop production declining by 36 per cent. Consequently, the state of emergency on crop production and food shortages was declared by the Government of Lesotho.

Figure 1: Recent Trends in Agriculture



Source Data: BOS

A number of factors have, and are still contributing to the dismal performance in agriculture as stated above. In respect of crops, the major factors are droughts and erratic rainfall, possibly due to climate change, land degradation resulting from rampant soil erosion and uncontrolled human settlements, the land tenure system, loss of interest on farming due to expensive inputs and low returns, and bad farming practices. In the case of livestock, the major impediment has been stock theft and poor management of livestock.

Review and assessment of major policies previously undertaken by MAFS

The MAFS has, over the years, developed and articulated several policies and strategies. The leading and broad strategy was the 2003 Agricultural Sector Strategy and the more specific ones were Lesotho Food Security Policy (2005), Subsidies in the Agricultural Sector (2003), Block Farming, Agricultural Policy and Capacity Building Program (APCBP), and the Irrigation and Seed Policies (pending approval by cabinet). Over and above these policies, there are several other studies that were conducted by, amongst others, FAO and NUL-CONSULS.

Despite all these initiatives, the agriculture subsector continues to decline. This does not mean that the research informing the policy formulation and strategies is not good. In fact, most of these policies are generally assessed as good, but the way they have been implemented and the institutional framework within which they are implemented are often suspect. Other issues like poor communication, less encompassing policies and financial constraint are among the reasons for ineffectiveness of the agricultural projects.

Overview of the Forum

The forum was intended to achieve the following: review the performance of the agricultural sector and map out ways and means for improving the situation; to facilitate critical reflections on key issues and experiences to generate lessons and build a broad consensus; to provide the strategic direction for future investment in agriculture and the development of the rural economy; and to build a general consensus amongst various stakeholders on the need to establish a platform to promote the exchange of ideas and relevant experiences on a regular and continual basis. Therefore, the final output of the forum is a report that identifies the main policy issues and financing gaps with prioritised solutions along with clarifying institutional arrangements and respective roles for effective implementation of strategies and activities.

The forum reviewed the general performance of the agriculture subsector and deliberated on its strengths, binding constraints, opportunities and threats. These were viewed in line with previous experiences, negative or otherwise, and how they could be carried forward as lessons learned for future investment in agriculture and the development of the rural economy.

The key strengths for the entire agriculture sector were identified as organised farmer groups, access and availability of skills, presence of some good policies and studies, presence of decentralised services at district and area-based levels, conducive climate for high cash crops and plenty of clean water. If taken advantage of and utilised efficiently, these factors could turn agricultural production around.

On the other hand, the following were marked as key weaknesses to the sector: technical and institutional weaknesses, poor marketing and market infrastructure, poor execution of some of the major initiatives, budgetary constraints, land tenure system, poor access to technology and to finance, and poor distribution of subsidies. These constraints need to be addressed and specific attention should be given to the most binding ones as identified by the forum.

On the bright side, the forum marked the following as opportunities to be exploited: irrigation and fisheries potential, organic food production, donor support and commercial grain production. Traditionally, grain production and cattle farming for subsistence purposes has dominated the way farming has been practiced in Lesotho. However, there is need for a shift towards other high value cash crops and other practices like fishing mainly for commercial purposes in order to generate incomes for the poor.

Finally, the following were noted as potential threats to the sector; theft, drought and erratic rainfall, HIV/AIDs, political influences in programmes, skilled labour migration, land degradation, cheap produce from outside and lack of motivation and commitment on the part of farmers and MAFS's staff. Theft remains the major threat for both livestock and crops and need immediate attention as it hinders more private investment in agriculture.

Priority Areas for Investment

Based on extensive deliberations on the issues above, the forum identified five key priority areas for investment in agriculture. The first area is the national household food security programme, wherein, promotion of conservation agriculture, smallholder irrigation and supply of inputs to increase soil productivity are key. The second area is the national irrigation revitalisation and development programme. In the third area, the forum called for public partnership framework to develop integrated supply and value chain cereals, potatoes, poultry, dairy, and wool and mohair.

The fourth area calls for participation of private sector led agricultural inputs production and marketing system development. This area emphasises enhancement of seed production, standards, as well as marketing and efficient procurement systems for agricultural inputs. The last area identified in the list of priorities is the national agricultural finance and market risk management programme.

Out of the above areas and other sub programmes, shall emerge a fully fleshed set of activities and the action plan in which role players will be clearly identified and time frames against which each player shall be monitored will be set. The monitoring will be done regularly by a special committee which will in turn provide feedback to all identified stakeholders.

Conclusion

The forum sets itself apart from the previous initiatives in that it is not a policy per say but a consensus culminating from a series of extensive debate and deliberations from all key stakeholders. It is, therefore, all encompassing, covering the agricultural sector and all key stakeholders. Most policies have been specific on certain areas. It also draws on previous experiences identifying what worked, what did not, shortfalls and the way forward. Agriculture is a very important sector in the economy and the forum can be the key to higher, sustainable and broad based economic growth and employment.

3. Monetary Policy Operations Report for May, 2010

In the review period, monetary policy operations undertaken by the Central Bank of Lesotho (CBL) were successful in attaining the desired objectives. The primary objective of the CBL's monetary policy is to achieve and maintain price stability. The Bank employs Open Market Operations (OMO) to achieve the stated objective. This initiative enables the Bank to maintain parity between the local currency, Loti, and the South African Rand, which is important for price stability.

This report presents economic and operational issues surrounding the monetary policy operations conducted during the month of May, 2010 to assess the success of the operations. Table 1 below shows the amounts auctioned and the discount rates that prevailed for each of the auctions during the review month. It shows that the entire amount of treasury bills (M40.0 million) announced during the auction conducted in May 12, 2010 was ultimately issued.

The 91-day treasury bills' market continued to perform satisfactorily. Competitiveness of the 91-day treasury bills auction (measured in terms of: number of bidders and bids received; over/under subscription of the auction; the spread of bidding prices; and the movement of discount rates) improved during the review period. Over-subscription increased from M19.6 million to M24.1 million. The 91day treasury bills' discount rate declined by 2 basis points to 6.4 per cent while the spread of bidding prices narrowed to M0.03 in the period under review compared with M0.13 realized in April. In addition the number of bidders fell from 7 to 3 in the review period while the number of bids declined to 3 from 7 realized in April 2010.

Table 1: Treasury Bills Auctions

Type of Security	Auction Date	Maturity Date	Auction Amount (Million Maloti)	Amount Issued (Million Maloti)	Over/(under) Subscription (million)	Discount Rate (%)	RSA Discount Rate (%)
91-day	12-May-10	11-Aug-10	M12.0	M12.0	M24.1	6.40%	6.59%
182-day		10-Nov-10	M12.0	M12.0	M13.0	6.63%	6.49%
273-day		09-Feb-11	M8.0	M8.0	M12.3	7.39%	6.54%
364-day		11-May-11	M8.0	M8.0	M10.7	7.50%	6.49%
Total for reporting period			M40.0	M40.0	M60.1		

During the review month, the intermediate target, Lesotho's 91-day treasury bills' rate (TBs discount rate) declined by 2 basis points to 6.4 per cent. Meanwhile, the spread of the bidding prices narrowed down to M0.03 in May compared with M0.13 realized in the last auction in April, 2010.The South African counterpart also declined but by 1 basis point to 6.59 per cent in May 12, 2010. As a result, the margin between the two rates widened further by 19.0 per cent in the review period compared to 18.0 per cent in the previous month. Lesotho's 91-day treasury bills' discount rate continued to remain below the South African counterpart in May, 2010.